United States Court of Appeals

for the Second Circuit

SUPPLEMENTAL BRIEF

74-2131

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

MILDRED IVES, MOIRA ROBERTSON & JOYCE CHAPMAN,
on behalf of themselves and others similarly situated,
Plaintiffs-Appellees,

vs.

W. T. GRANT COMPANY,
Defendant-Appellant.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF CONNECTICUT

SUPPLEMENTAL REPLY BRIEF OF DEFENDANT-APPELLANT

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I.

Introduction

This brief is submitted by the defendant in reply to the brief *amicus curiae* submitted by the Federal Reserve Board on April 4, 1975. In this brief the defendant will confine its arguments to those claims made by the Federal Reserve Board which were not previously made by the plaintiffs. The defendant's basic position is stated in its brief dated October 24, 1974 and in its reply brief dated January 17, 1975.

II.

The Federal Reserve Board Has No Power Under 15 U.S.C. § 1633 to Grant a Partial Exemption

The argument of the Federal Reserve Board (hereinafter referred to as the "FRB") that the clause "requirements of this chapter" contained in § 1633 does not include the requirements of § 1640 is not persuasive. Section 1633 provides:

> The Board shall by regulation exempt from the *requirements* of this chapter any class of credit transactions within any State if it determines that under the law of that State that class of transactions is subject to *requirements* substantially similar to those imposed under this chapter, and that there is adequate provision for enforcement. (Emphasis added).[1]

The word "requirements" is used twice in § 1633 and, from the context, it is clear that when used the second time it was intended to have a narrower meaning than when first used. When used the second time, it clearly means the *disclosure requirements* of state law which are applicable to the *exempted* class of transactions. When used the first time, it means all the requirements of chapter 2 of the Federal Act which are applicable to *non-exempted* transactions. The "requirements of this chapter" include requirements other

[1] In their prior briefs, both the defendant and the plaintiffs cited to and quoted from the Truth-in-Lending Act (hereafter referred to as the "Act") as incorporated in Title 15 of the United States Code. In its brief the FRB quotes from the Act as it appears in Pub. Laws 90-321 and 93-495. For ease of reference, in this brief the defendant will quote from the Act as it appears in the Public Laws. The only differences between the Code version and the Public Laws are that the Code uses the word "part" in place of the word "chapter" and the words "Part B" in place of the words "Chapter 2". Title 15 of the Code has not as yet been enacted into law.

than disclosure requirements, including the requirement contained in § 1640 that a creditor respond in damages if he fails to disclose the information required to be disclosed.

Chapter 2 also includes § 1634 which provides:

> If information disclosed in accordance with this chapter is subsequently rendered inaccurate as the result of any act, occurrence, or agreement subsequent to the delivery of the required disclosures, the inaccuracy resulting therefrom does not constitute a violation of this chapter.

Section 1634, like § 1640, does not contain any *disclosure* requirements. However, the FRB included § 1634 among the sections from which Connecticut was exempted.

The distinction the FRB *now* seeks to draw between "requirement" and "remedy" just does not exist. The word "remedy" does not appear anyplace in Chapter 2 of the Act or in the applicable Regulation of the FRB. Section 1640 is entitled "Civil liability" and the FRB used this terminology in 12 C.F.R. § 226.12(c) when it attempted to create federal jurisdiction over state law claims:

> (c) In order to assure that the concurrent jurisdiction of Federal and State courts created in section 130(e) of the Act shall continue to have substantive provisions to which such jurisdiction shall apply, and generally to aid in implementing the Act with respect to any class of transactions exempted pursuant to paragraph (a) of this section and Supplement II, the Board pursuant to sections 105 and 123 hereby prescribes that:
>
> (1) No such exemption shall be deemed to extend to the civil liability provisions of sections 130 and 131; . . .

Obviously, when the FRB promulgated 12 C.F.R. § 226.12(c) it construed the phrase "requirements of this chapter" in

§ 1633 to include the civil liability provisions of § 1640. Otherwise, the first clause in § 226.12(c)(1), cited above, and the convoluted and laborious structure of § 226.12(c) would not have been necessary. The FRB merely would have stated in the regulation that the exemption shall not extend to § 1640 because § 1633 does not empower the FRB to exempt credit transactions from the civil liability sections of the chapter. The issue is not whether concurrent jurisdiction is desirable, as the FRB would frame it; but whether § 1633 empowers the FRB to issue partial exemptions. The plain meaning of that section, the entire Truth-in-Lending Act, and the legislative history of the Act is that partial exemptions are not authorized and were never contemplated.

Section 1633 *requires* the FRB to exempt a class of credit transactions within a state from all, not some, of the requirements of Chapter 2, once the FRB determines that, under the law of that state, the class of credit transactions is subject to requirements substantially similar to those imposed under Chapter 2 of the Federal Act and that there is adequate provision for enforcement. On July 20, 1970, the FRB granted Connecticut an exemption from the Federal Truth-in-Lending Act. 35 Fed. Reg. 11992 (July 25, 1970). The plaintiffs have made no claim that the Connecticut law does not contain requirements substantially similar to those imposed under Chapter 2 of the Federal Act or that there is not adequate provision for enforcement.[2] Therefore, § 1640, which is part of Chapter 2, does not provide a basis for federal subject matter jurisdiction over the state law claims made by the plaintiffs in this case.

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[2] The FRB claims that if the Court were to determine that there is no federal jurisdiction over state law claims, the exemption must fail because the FRB did not review Connecticut civil procedure prior to granting it. As to this claim, see discussion in part IV below.

III.

15 U.S.C. § 1640 Does Not Create Federal Subject Matter Jurisdiction Over Claims Arising Under the Law of the State of Connecticut

The FRB's basic position, stated in Section II, Part B of its brief, is that it has broad regulatory authority to interpret the Act and effectuate its purposes and that 12 C.F.R. § 226.12(c) is a valid exercise of that authority. It is so that the FRB has broad regulatory authority, but that broad authority does not extend to defining the subject matter jurisdiction of the federal courts. It is axiomatic that federal courts are courts of limited jurisdiction and have no jurisdiction, except as granted by Congress. It is significant that in its brief the FRB does not point to a single statute to support its claim that there is federal subject matter jurisdiction over claims arising under the laws of the State of Connecticut. Not only is there no such statutory authority, but § 1640 by its own terms does not extend federal subject matter jurisdiction to claims arising under state law. Section 1640, as amended by Pub. L. 93-495, provides in relevant part:

> (a) Except as otherwise provided in this section, any creditor who fails to comply with any *requirement imposed under this chapter* or chapter 4 of this title with respect to any person is liable to such person. . . .
>
> * * * *
>
> (e) Any action under *this section* may be brought in any United States district court, or in any other court of competent jurisdiction, within one year from the date of the occurrence of the violation. (Emphasis added)

Thus, the federal subject matter jurisdiction created by § 1640 extends only to actions against a "creditor who fails to comply with any requirement imposed under this

chapter". However, with three exceptions not relevant in this case, all classes of credit transactions in Connecticut have been exempted from the "requirements" of Chapter 2 of the Act. The operative regulation provides in its entirety:

> *Connecticut:* Except as provided in § 226.12(c), all classes of credit transactions within the State of Connecticut are hereby granted an exemption from the *requirements of Chapter 2 of the Truth in Lending Act* effective August 1, 1970, with the following exceptions:
>
> (1) Transactions in which a Federally chartered institution is a creditor;
>
> (2) Consumer credit sales of insurance by an insurer;
>
> (3) Transactions under common carrier tariffs in which the charges for the services involved, the charge for delayed payment and any discount allowed for early payment are regulated by a subdivision or agency of the United States or the State of Connecticut. (Emphasis added)
> 35 Fed. Reg. 11992

Thus, as of August 1, 1970, all classes of credit transactions in Connecticut were exempt from "the requirements of Chapter 2." Section 1640, however, creates federal subject matter jurisdiction only for actions for failure to comply with the requirements of Chapter 2. This case is not an action alleging a failure to comply with the requirements of Chapter 2; in Counts I and II of their Complaint, the plaintiffs allege only that the defendant failed to provide the disclosures required by "Section 36-395 of the Connecticut General Statutes and the regulations thereunder . . ." (App. 15a-17a) Therefore, the District Court did not have subject matter jurisdiction over the truth in lending

claims in this case pursuant to § 1640(e). On this point the statute is clear.[3]

Despite the clear and unambiguous language of the Act, the FRB promulgated 12 C.F.R. § 226.12(c) which provides in its entirety:

> (c) In order to assure that the concurrent jurisdiction of Federal and state courts created in section 130(e) of the Act shall continue to have substantive provisions to which such jurisdiction shall apply, and generally to aid in implementing the Act with with respect to any class of transactions exempted pursuant to paragraph (a) of this section and Supplement II, the Board pursuant to sections 105 and 123 hereby prescribes that:
>
> (1) No such exemption shall be deemed to extend to the civil liability provisions of sections 130 and 131; and
>
> (2) After an exemption has been granted, the disclosure requirements of the applicable State law shall constitute the disclosure requirements of this Act, except to the extent that such State law imposes disclosure requirements not imposed by this Act. Information required under such State law with the exception of those provisions which impose disclosure requirements not imposed by this Act shall, accordingly, constitute the "information required under this Chapter" (Chapter 2 of the Act) for the purpose of section 130(a).

Thus, in order to avoid the natural and inevitable result of exclusive state jurisdiction upon the granting of an ex-

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[3] Moreover, this is so even if one accepts the FRB's strained construction of the term "requirements" since the same term appears in § 1640, § 1633 and 12 C.F.R. § 226.12—Supplement III(e).

emption pursuant to § 1633,[4] the FRB took it upon itself to provide that "the disclosure requirements of the applicable State law shall constitute the disclosure requirements of this Act. . . ." The issue in this case is simply whether the FRB had the power to thus adopt state law as the law of the United States.

In its brief the FRB cites no statute, case or legislative history to support its claim that it has the power to adopt state law as federal law. If Congress had intended such an unusual result it would have expressed its intention in clear and unambiguous language. Although the incorporation (or absorption) of federal law into state law is commonplace, *see, e.g., Note, Supreme Court Review of State Interpretations of Federal Law Incorporated by Reference,* 66 HARV. L. REV. 1498 (1953), Congress has rarely incorporated state law by reference into federal law, except in special situations, such as the Federal Tort Claims Act, where state law is applied, see 28 U.S.C. § 1346(b), and in tax and criminal statutes where state

[4] It should be noted that § 226.12(c) does not even by its terms purport to preserve concurrent jurisdiction over truth-in-lending claims. That section provides for the incorporation of state disclosure requirements as federal requirements "except to the extent that such State law imposes disclosure requirements not imposed by this Act". Thus, even the FRB recognizes that § 1640 does not provide for federal jurisdiction over additional disclosure requirements imposed by a State. Connecticut, for example, requires disclosure of the "address and telephone number where inquiries may be directed". Connecticut General Statutes § 36-404(b)(11), § 36-405(a)(11), and § 36-406(a)(9). The federal act does not contain such a requirement. Not only does § 226.12(c) fail to preserve concurrent jurisdiction, it also creates a risk of double exposure to a creditor on a single disclosure form. That section permits a federal action for violation of state disclosure requirements incorporated into federal law, but not for those not so incorporated. Thus, a debtor could sue in the federal court for failure to comply with the incorporated disclosure requirements and at the same time sue in the state court for failure to comply with the non-incorporated disclosure requirements. Congress did not intend this result.

law is often used to obtain definitions. *e.g.*, 18 U.S.C. §§ 13, 1153. *See,* Hart & Wechsler, *The Federal Courts and the Federal System* 491-494, 768 (2d Ed. 1973); Hart, *The Relations Between State and Federal Law,* 54 COLUM. L. REV 489, 529-530 (1954).

Research discloses only one statute where Congress has broadly adopted state law by reference, thereby "absorbing" it into and making it federal law. Section 4 of the Lands Act, 43 U.S.C. § 1333, provides in relevant part:

> (a)(2) To the extent that they are applicable and not inconsistent with this subchapter or with other Federal laws and regulations of the Secretary now in effect or hereafter adopted, *the civil and criminal laws of each adjacent State as of August 7, 1953 are declared to be the law of the United States* for that portion of the subsoil and seabed of the outer Continental Shelf, and artificial islands and fixed structures erected thereon, which would be within the area of the State if its boundaries were extended seaward to the outer margin of the outer Continental Shelf. . . . All of such applicable laws shall be administered and enforced by the appropriate officers and courts of the United States. . . .
>
> (3) The provisions of this section for *adoption of State law as the law of the United States* shall never be interpreted as a basis for claiming any interest . . . on behalf of any state for any purpose over the seabed and subsoil of the outer Continental Shelf . . . (Emphasis added)

Thus, Congress expressed its desire to adopt state law as federal law in language which is clear and explicit. The Senate Report referred to the "precise unequivocal language" of "the provision for the adoption of State laws as Federal law," S. Rep. No. 411, Committee on Interior

and Insular Affairs, 83d Cong., 1st Sess., 11 (1953), cited in *Rodrigue* v. *A[illegible]ia Casualty & Surety Co.*, 395 U.S. 352, 357 (1969). "The principles that federal law should prevail, and that state law should be applied only as federal law and then only when no inconsistent federal law applied, were adopted by a Congress in which full debate had underscored the issue." 395 U.S. at 358. Also *see Chevron Oil Co.* v. *Huson*, 404 U.S. 97, 102-03 (1971).

In light of the fact that federal courts are courts of limited jurisdiction (refer to discussion in defendant's original brief at pages 16-17), if Congress had intended to incorporate the state law into the Federal Act, it would have done so in clear and explicit language as it did in the Lands Act. Since the FRB had no power to incorporate state law into federal law by reference, § 226.12(c) is void and of no effect in so far as it purports to do so.

IV.

The Exemption Granted Connecticut is Valid Even if 12 C.F.R. § 226.12(c) is Invalid

The position of the FRB seems to be that, if there is not concurrent jurisdiction, there cannot be any exemption pursuant to § 1633. An analysis of the statute discloses no support for this position. Indeed, the entire statutory scheme, as discussed above, is to create exclusive state jurisdiction of state law claims.

The FRB's basic argument seems to be that Congress required it do something it has no expertise to do, that is "to undertake a comparative analysis of the procedural rights granted under various state procedural codes with those granted under the Federal Rules of Civil Procedure" (FRB brief pp. 27-28) The statute contains no such requirement. Section 1633 merely requires the FRB to determine if "there is adequate provision for enforcement." The statute contains no mention of "procedural

rights'' much less any requirement that the FRB compare the ''procedural rights'' under the various state codes with those of the Federal Rules of Civil Procedure.[5] Indeed not even the drafters of regulations at the FRB, as opposed to the FRB brief writers, read § 1633 as requiring a comparative analysis of the state codes of civil procedure with the Federal Rules of Civil Procedure. The procedures and criteria under which any state may apply for exemption pursuant to § 1633 are set forth in 12 C.F.R. § 226.12—Supplement II(c)(3) which provides:

> (3) In determining whether provisions for enforcement of State law referred to in subparagraph (1) of paragraph (b) is [sic] adequate, consideration will be given to the extent to which, under the laws of the State, provision is made for:
>
> (i) Administrative enforcement, including necessary facilities, personnel and funding;
>
> (ii) Criminal liability for willful and knowing violation with penalties substantially similar to those prescribed under §112 of the Act;
>
> (iii) Civil liability for failure to make required disclosures substantially similar to those provided under § 130 and § 131 of the Act, except that more severe penalties may be provided; and
>
> (iv) A statute of limitations with respect to civil liability of substantially similar duration as that provided under §130 of the Act.

Thus, neither Congress in §1633 nor the FRB in its regulations implementing §1633 intended that the FRB, in determining if there is ''adequate provision for enforcement'', conduct an analysis of the ''procedural rights'' available under the various state procedural codes.

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[5] Moreover, contrary to the view of the FRB, Connecticut procedure does provide for class actions. The relevant provisions are contained in §§ 52-105 and 42-110g—42-110i of the Connecticut General Statutes and § 52 of the Connecticut Practice Book.

Neither the plaintiffs nor the FRB claims that the Connecticut Truth-in-Lending Act fails to meet any of the criteria established by 12 C.F.R. §226.12—Supplement II (c)(3). Indeed an analysis of the Connecticut Truth-in-Lending Act demonstrates that the FRB was correct in determining that the act met all the relevant criteria.[6]

The exemption, therefore, must stand without the offending limitations as was intended by Congress. Section 501 of the original Act, Pub. L. 90-321, provides in relevant part:

> [i]f a provision enacted by this Act is held invalid in one or more of its applications, the provision remains in effect in all valid applications that are severable from the invalid application or applications.

Here, as pointed out by defendant at pages 4-5 of its Reply Brief, the offending *limitation* on the exemption is mere surplusage, since the Congressional mandate is to issue an exemption whenever the FRB determines, as it did here, pursuant to an otherwise valid and complete regulation, that the state law is "substantially similar" to federal law and there is adequate provision for enforcement.[7]

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[6] Section 36-414 provides for administrative enforcement by an existing State agency; §36-399, for criminal penalties; and §36-407, for civil liability and a statute of limitations.

[7] The argument of the FRB that there is federal subject matter jurisdiction, pursuant to 28 U.S.C. §1337, over truth-in-lending claims arising under the law of the State of Connecticut is absolutely without merit. 28 U.S.C. §1337 provides:

> The district courts shall have original jurisdiction of any civil action or proceeding *arising under any Act of Congress* regulating commerce or protecting trade and commerce against restraints and monopolies. (Emphasis added)

Assuming arguendo that §1337 creates federal subject matter jurisdiction over actions alleging a violation of the *federal* act, it obviously does not provide such jurisdiction over an action alleging a violation of a *state* truth-in-lending act. The cases of *Sosa* v. *Fite*, 465 F.2d 1227 (5th Cir. 1972) and *Littlefield* v. *Walt Flanagan and Company*, 498 F.2d 1133 (10th Cir. 1974), cited by the FRB in support of this claim, are inapposite. Each of these cases involved alleged violations of the federal Act in states which had not been exempted.

Conclusion

For the foregoing reasons it is respectfully submitted that Congress did not grant the FRB the power to issue partial exemptions and, therefore, that 12 C.F.R. § 226.12(c) is void and of no force or effect. However, 12 C.F.R. § 226.12—Supplement III(e) is, except for the reference to § 226.12(c), a valid exercise of the power granted to the FRB pursuant to 15 U.S.C. § 1633 and the Connecticut exemption is valid. Since there is no federal subject matter jurisdiction over this action for failure to comply with the disclosure requirements of the Truth-in-Lending Act of the State of Connecticut, the action should be remanded to the District Court with instructions to dismiss if it finds no alternative ground of federal jurisdiction.

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ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF CONNECTICUT

Affidavit of Service by Mail

STATE OF NEW YORK
COUNTY OF New York } ss.:

Robert McElroy , being duly sworn, deposes and says:

I am over the age of twenty-one years and reside at 32 Gramercy Park South , in the Borough of Manhattan , City of New York. On the 18th day of April , 19 75 , at 11:00 o'clock a.m.,

I served 2 copies of the Supplemental Reply Brief of Defendant-Appellant

in the above-entitled action on each of the following parties:

William H. Clendenen
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the attorney for the

in the said action, by depositing said copies, securely wrapped, properly addressed, and postage fully prepaid, in a post office box regularly maintained by the U. S. Government in the post office at 90 Church Street, in the Borough of Manhattan, City of New York.

Robert McElroy

Sworn to before me this
18th day of April, 1975

Michael J. Hoops

MICHAEL J. HOOPS
Notary Public, State of New York
No. 30-4503056
Qualified in Nassau County
Commission Expires March 30, 1977